

Message Text

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ACTION NEA-10

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C O N F I D E N T I A L TEL AVIV 8750

E. O. 11652: GDS
TAGS: EFIN IS
SUBJ: PERIODIC ECONOMIC POWWOW

1. SUMMARY: TOP MINISTRY OF FINANCE AND BANK OF ISRAEL OFFICIALS MET FOR TWO DAYS THIS PAST WEEK TO REVIEW THE ECONOMIC SITUATION AND SET THE FRAMEWORK FOR THE SUPPLEMENTARY GOVERNMENT BUDGET. ACCORDING TO PRESS REPORTS VERIFIED BY MINISTRY OF FINANCE OFFICIALS, TOTAL FY 78 GOVERNMENT SPENDING WILL BE IL 204 BILLION (IL 25 BILLION ABOVE THE ORIGINAL BUDGET) AND THE DEFICIT WILL BE IL 10 BILLION. MINISTER OF FINANCE EHRlich STATED FOLLOWING THE MEETING THAT HE WAS CONFIDENT THAT THE COST OF LIVING (COL) INCREASE WOULD BE HELD TO 33 PERCENT ON A JANUARY THROUGH DECEMBER BASIS. END SUMMARY

2. THE MINISTER OF FINANCE, THE GOVERNOR OF THE BANK OF ISRAEL AND THEIR TOP ASSISTANTS MET JULY 2 AND 3 TO ANALYZE THE ECONOMIC SITUATION AND MAKE APPROPRIATE CHANGES IN ECONOMIC POLICIES. THE MEETING WAS DEVOTED PRIMARILY TO FORMULATING SUPPLEMENTARY BUDGET GOALS TO REFLECT THE PUBLIC SECTOR WAGE AGREEMENTS, THE ANTICIPATED RATE OF INFLATION FOR THE FISCAL YEAR, AND A REALISTIC RATE OF EXCHANGE OF THE DOLLAR TO THE ISRAELI POUND.

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3. ACCORDING TO PRESS ACCOUNTS VERIFIED BY A MINISTRY OF FINANCE OFFICIAL, THE SUPPLEMENTARY BUDGET WILL RAISE TOTAL EXPENDITURES FOR THE FISCAL YEAR TO IL 204 BILLION FROM IL 179 BILLION. THE INCREASE OF IL 25 BILLION IS ATTRIBUTED TO THE WAGE AGREEMENT WHICH INCREASED WAGE PAYMENTS BY SOME 15 PERCENT, A CHANGE IN THE PROJECTED EXCHANGE RATE OF THE DOLLAR TO THE POUND, HIGHER COSTS

FOR GOODS AND SERVICES BECAUSE OF THE USE OF A UNREALISTICAL-
LY LOW RATE OF INFLATION IN THE ORIGINAL BUDGET, AND A
DOUBLING OF THE BILL FOR SUBSIDIES AS A RESULT OF THE
WAGE AGREEMENT. ALTHOUGH THERE WILL BE NO NEW TAXES,
THE MINISTRY OF FINANCE ESTIMATES THAT THE DEFICIT WILL IN-
CREASE ONLY BY SOME IL 3.5 BILLION FROM IL 6.5 BILLION
IN THE ORIGINAL BUDGET TO IL 10 BILLION, AND THAT THE 1978
LIQUIDITY INJECTION WILL BE LOWER THAN LAST YEAR'S
IL 9 BIL-
LION. THE DEFICIT WILL BE HELD DOWN BECAUSE OF HIGHER TAX
COLLECTIONS DUE TO HIGHER PERSONAL INCOMES AND
HIGHER THAN EX-
PECTED GROWTH IN THE ECONOMY.

4. THE MINISTRY OF FINANCE NOW PROJECTS THE AVERAGE
RATE OF EXCHANGE FOR THE DOLLAR DURING THE FISCAL
YEAR WILL BE 19 POUNDS TO THE DOLLAR AND BY THE END OF
THE FISCAL YEAR (MARCH 1979) THE RATE WOULD BE 21.5
POUNDS TO THE DOLLAR. THIS ACCOUNTING ADJUSTMENT IS RE-
SPONSIBLE FOR ABOUT IL 7 BILLION POUNDS OF THE INCREASE
IN THE BUDGET; ALTHOUGH IT HAS NO REAL EFFECT ON REVENUES
OR EXPENDITURES.

5. EHRLICH, IN AN INTERVIEW FOLLOWING THE MEETING, IN-
SISTED THAT THE COL WOULD BE HELD TO 33 PERCENT ON A
JANUARY THROUGH DECEMBER BASIS AND 43 PERCENT WHEN COM-
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PARING THE YEARLY AVERAGE OF 1978 WITH THE AVERAGE FOR
1977.

6. COMMENT: IT IS DOUBTFUL THAT THE GOI WILL BE ABLE TO
HOLD SPENDING DOWN TO IL 204 AND THE DEFICIT TO IL 10 BIL-
ION. THE DEFICIT MORE LIKELY WILL BE IN THE IL 13-15 BIL-
LION RANGE, ROUGHLY THE SAME LEVEL AS LAST YEAR IN REAL
TERMS. ON THE INFLATION SIDE, IF THE PUBLIC WAGE SECTOR
AGREEMENTS ARE SIGNED ON THE BASIS OF THE GENERAL AGREE-
MENT, THE RISE IN THE COL COULD AMOUNT TO LESS THAN 35 PER-
CENT ON A JANUARY THROUGH DECEMBER BASIS; BUT WE BELIEVE
OUR EARLIER ESTIMATE OF A RISE OF 35-40 PERCENT IS MORE
PROBABLE. THE EXCHANGE RATES NOW PROJECTED FOR THE POUND
OF 19 POUNDS TO THE DOLLAR AS AN AVERAGE FOR THE FISCAL
YEAR AND 21.5 POUNDS FOR THE DOLLAR FOR FISCAL YEAR END ARE
REASONABLE. THE EXCHANGE RATE FORECAST APPEARS TO BE A
STRAIGHT LINE TREND OF THE FIRST QUARTER. LEWIS

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